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INTRODUCTION

In accordance with the City Auditor's 1995-96 Audit Workplan, we have audited the San Jose Arena Management Agreement by and between the city of San Jose and the San Jose Arena Management Corporation. We conducted this audit in accordance with generally accepted government auditing standards and limited our work to those areas specified in the Scope and Methodology section of this report.

The City Auditor's Office thanks the San Jose Arena Authority and those individuals in the San Jose Arena Management Corporation who gave their time, information, insight, and cooperation during the audit process.

BACKGROUND

On December 17, 1990, the city of San Jose (City), the city of San Jose Redevelopment Agency (Agency), and the San Jose Arena Management Corporation (SJAMC) signed a letter of agreement. That agreement outlined the terms and conditions that were to be negotiated in good faith to arrive at formal agreements relating to the construction, management, and maintenance of a first class, multi-purpose, hockey-ready entertainment and sports facility and adjacent parking facilities.

Subsequently, the City, the Agency, and the SJAMC entered into two agreements: (1) the San Jose Arena Agreement To Enter and (2) the San Jose Arena Management Agreement. The first agreement coordinated the design and construction of the Arena facilities. The second agreement covers the operation and management of the Arena facilities. Our audit addresses the San Jose Arena Management Agreement.

The San Jose Arena Management Agreement

The City and SJAMC entered into the San Jose Arena Management Agreement (Agreement) on October 24, 1991. The term of the Agreement is to July 31, 2008. The SJAMC took possession of the building on August 20, 1993, which is considered the first term year. Therefore, the length of the Agreement is for 15 years. The SJAMC has three five-year options to extend the terms of this Agreement. The purpose of the Agreement is to set forth the rights and obligations of the City and the SJAMC with respect to the management and operation of the Arena facilities.

The City's Goals And Objectives

As stated in the Agreement, the City's goals and objectives are:

- 1. To optimize the use of the Arena Facilities and its revenue-gathering capacities while minimizing the net cost to City and avoiding City exposure to operating losses;*
- 2. To obtain as an immediate objective a National Hockey League (the "NHL") professional hockey franchise known as the "San Jose Sharks" to play its home games in the Arena . . . ;*
- 3. To stimulate the economy of the community;*
- 4. To protect the capital investment in the Arena Facilities through exercise of maintenance equal to the Applicable Standard;*
- 5. To promote the design and construction in all additions and alterations to the Arena Facilities equal to the Applicable Standard; and*
- 6. To provide facilities and opportunities for groups and organizations from outside the greater San Jose community.*

The San Jose Arena Management Corporation

Subject to the terms of the Agreement, the City engaged the SJAMC as an independent contractor with the sole responsibility and right to operate, manage, and maintain the Arena facilities. The SJAMC's sole authority is subject to (1) the terms of the Agreement and (2) applicable laws and governmental regulations. Under the Agreement, the SJAMC has the responsibility and authority for, but is not limited to, the following areas:

- A. Employ or contract for such workers, mechanics, laborers, clerks, legal counsel, consultants, accountants and other employees and contractors as are reasonably necessary or appropriate in the management and operation of the Arena Facilities;*
- B. Procure such materials, services, public utility services, supplies and equipment as are reasonably necessary or appropriate in the management and operation of the Arena Facilities, consistent with the terms of this Management Agreement;*

- C. *Procure and maintain in force and effect public liability, workers' compensation, and such other insurance and bonds as are required of Manager . . . ;*
- D. *Purchase or otherwise acquire, hold, own, sell, lease, hypothecate, convey, exchange, option or otherwise dispose of Manager's personal property of every class and description and any estate or interest therein used in the operation of the Arena Facilities, for any reasonable purpose consistent with this Management Agreement;*
- E. *Lease, license, rent, use or permit the use of all or any part of the Arena, to any person or entity, for events consistent with the terms of this Management Agreement, the City Policies and Guidelines which may be established pursuant to Section 3.01 hereof and the use of the Arena as major public assembly facilities . . . ;*
- F. *Operate or grant concession privileges for the vending and sale of food and beverages, including alcoholic beverages, programs, cushions, souvenirs, novelties, retail merchandise and similar articles, and other articles, or for the renting of any such articles, consistent with the terms of this Management Agreement . . . ;*
- G. *Take and omit such other actions, enter into such other agreements, documents, and instruments, and engage in such other transactions, as are reasonably necessary or appropriate in connection with the management, operation, maintenance, improvement and administration of the Arena Facilities . . . ; and*
- H. *Administer all existing and future leases, licenses, use agreements, bookings, concession agreements, advertising, and scoreboard agreements related to the Arena Facilities, except as otherwise specifically provided herein. Subject to the provisions of, and except as otherwise provided in, this Management Agreement, Manager shall have the sole and exclusive right to sell Arena or ticket advertising, and to permit, license, or engage in the broadcast or transmission of all or any part of an Arena event.*

The San Jose Arena Authority

In June 1990, the City Council and the Redevelopment Agency Board approved the creation and funding of the San Jose Arena Authority (SJAA). Section 1.03 of the Agreement discusses the SJAA and states,

City has established the Arena Authority, whose purposes include performing an oversight role respecting the operation of the Arena

Facilities on behalf of City and acting as a liaison to the broader community concerning neighborhood impacts and the operation of the Arena Facilities.

In February 1992, the City and the Agency entered a "Restated Agreement" which describes in detail the two major areas for which the SJAA is responsible. Those two major areas of responsibility are to (1) oversee the SJAMC's operation of the Arena through interpretation and the application of the terms and provisions of the Agreement and (2) monitor and develop relations with the community with respect to impacts from the operation of the Arena. In addition, the Restated Agreement lists the following services that the SJAA is to perform:

- 1. Supervise the Manager's operation of the Arena project during construction on behalf of the AGENCY'S Board of Directors.*
- 2. Supervise the operation of the Arena Facilities on behalf of the City Council of San Jose.*
- 3. Monitor and review the performance management and maintenance standards as set forth in the Management Agreement.*
- 4. Act as CITY'S liaison to the San Jose community concerning neighborhood impacts in the operation of the Arena facilities.*
- 5. Administer the Community Events Policy and CITY Events as set forth in the Management Agreement.*
- 6. Review all service and construction contracts to the extent authorized in the Management Agreement.*
- 7. Review all operating and capital budgets furnished by Manager as provided in the Management Agreement.*
- 8. Review all operating budgets submitted by Manager for review in accordance with the Management Agreement.*
- 9. Review and approve all capital budgets submitted by Manager for review in accordance with the Management Agreement.*
- 10. Oversee and review the disposition of the \$200,000.00 Capital Reserve Fund established under the Management Agreement.*
- 11. Receive annual audits from the Manager. Copies of such audits shall be furnished to the CITY and AGENCY.*

12. *Serve as the liaison between the Manager, the City Council and Agency Board.*
13. *Administer use of any executive suite or luxury box and tickets (including parking passes) provided to the CITY under the terms of the Management Agreement and in accordance with the policies for distribution as may be adopted by Council from time-to-time.*

Other Agreements

Since entering into the Agreement, various parties have entered into other agreements which affect certain provisions of the Agreement. These agreements are the Settlement Agreement and the Cooperation Agreement.

Settlement Agreement

On July 28, 1994, the City, the Agency, the SJAMC, and the San Jose Sharks entered into a Settlement Agreement. This agreement settled various disputes that had arisen between the various parties. The terms of the Settlement Agreement that are applicable to the various terms of the Management Agreement are as follows:

- The Agency and the City are fully released from any obligations to provide final parking and/or any obligation to provide additional on-site parking facilities arising from the Agreement to Enter beyond the on-site parking presently developed.
- The SJAMC agrees to assume responsibility for the off-site security arrangements pursuant to an agreement to be entered into between the SJAMC and the City in a form substantially as provided in Exhibit A of the Settlement Agreement. The Agency will have no involvement in the agreement for security.
- The SJAMC shall pay to the City the \$100,000 parking fee payment owed to the City since August 20, 1993.

- The SJAMC and the Sharks understand and acknowledge that the City and the Agency have no intention of selling the building name and the Arena will continue to be called the "San Jose Arena."

Cooperation Agreement

On March 20, 1995, the City and the Agency entered into a Cooperation Agreement that relates to the Arena. Pertinent terms of the Cooperation Agreement are as follows:

- The Agency will transfer title, possession, and control of the Arena to the City, and the City will accept such effective as of September 7, 1994;
- The Agency will indemnify the City for all costs required to correct design and workmanship deficiencies or premature failures of building components not covered by warranty which occur or are discovered during a two-year period from September 7, 1994 to September 7, 1996, including any costs associated with the pursuit of corrective actions, except to the extent that any deficiencies or premature failures are the result of the negligence of the SJAMC or the City; and
- The Agency will assist and cooperate with the City throughout the term of the Management Agreement to enable the City to satisfy any and all off-site parking requirements contained in the Management Agreement.

Major Accomplishments

In accordance with Section 4.G. of the agreement between the City, the Agency, and the SJAA, the SJAA submits an annual progress report to the City Manager and the Agency's executive director outlining all of the SJAA's accomplishments. In Appendix F, the SJAA informs us of its major accomplishments from its inception in 1990 to July 1995. According to the executive director of the SJAA, some of its major accomplishments are

- In coordination with the City and the Agency, oversaw the Arena's construction process;
- Assisted in the development of the City Arena Traffic and Parking Management Plan, including implementation of a successful, free-to-the-public Arena shuttle program;
- Planned and produced the grand opening for the Arena;
- Established and implemented a comprehensive community- and economic development-based Arena ticket distribution policy and program;
- Developed and established a City and Community Events program;
- Developed and implemented the San Jose Sports Hall of Fame program and produced the inaugural inductee ceremony in 1995;
- Approved a \$700,000 basketball improvement program for the Arena;
- Contracted with a joint venture consulting group for the implementation of a comprehensive Arena maintenance oversight program;
- Produced a one-year anniversary event for the San Jose Arena.

A full text of the SJAA's memorandum of accomplishments is shown as Appendix F to this report.

SCOPE AND METHODOLOGY

We reviewed the San Jose Arena Management Agreement (Agreement) between the city of San Jose (City) and the San Jose Arena Management Corporation (SJAMC). Based upon our review, we compiled a list of terms from the Agreement which we tested for compliance. See Appendix B for a list of the terms tested.

To determine compliance with the terms of the Agreement, we interviewed staff from the City Attorney's Office, the San Jose Arena Authority (SJAA), and the SJAMC. We reviewed the controls and procedures the SJAMC has in place as they relate to specific terms in the Agreement. We also reviewed the various agreements that the City, the SJAMC, and/or the Redevelopment Agency (Agency) have entered into from inception. In addition, we reviewed various sections of the agreements the SJAMC has with various contractors who provide cleaning, concession, security, and maintenance services for the Arena facilities.

We also reviewed various reports from the City, the SJAA, the SJAMC, the SJAMC independent auditors, and the contractors who provide the services noted above at the Arena. Furthermore, we reviewed City and SJAMC insurance policies and correspondence between all the parties noted as it relates to the terms of the Agreement that have compliance requirements.

Finally, from all the documents reviewed, we analyzed the information received to determine compliance with the Agreement terms subject to our audit.

FINDING I

THE CITY OF SAN JOSE AND THE SAN JOSE ARENA MANAGEMENT CORPORATION NEED TO PERFORM VARIOUS TASKS TO ENSURE COMPLIANCE WITH THE MANAGEMENT AGREEMENT

The San Jose Arena Management Agreement (Agreement) addresses the operation and management of the San Jose Arena facilities. Our audit focused on those areas of the Agreement that contain compliance requirements. Our review revealed 90 instances of compliance with the terms of the Agreement and 29 instances of noncompliance with the terms of the Agreement. In addition, we identified 28 terms for which compliance needs to occur at a future date. Table I summarizes the terms for which we found compliance and noncompliance with specific sections of the Agreement.

TABLE I

**SUMMARY OF COMPLIANCE OR
NONCOMPLIANCE WITH THE TERMS
OF THE AGREEMENT SUBJECT TO AUDIT**

Agreement Section	Section Name	Number Of Terms In Compliance	Number Of Terms Not In Compliance	Number Of Future Compliance Terms	Other
2.01	Term	0	1	0	0
3.03	NBA Or Other Professional Sports Team	0	1	0	1
4.01	In General	7	0	0	0
4.02	Operating Performance Standards	2	0	0	0
4.03	Limitation On Term Of Leases, Licenses, Contracts And Commitments	3	0	0	0
4.08	Maintenance Standard	1	1	0	0
4.09	Security And Security Personnel	1	0	0	1
4.11	Consultation Regarding Prices	1	0	0	1
4.12	Compliance With Laws By Manager	1	1	0	0
4.13	Compliance With Contemporary Community Standards	1	0	0	0
4.16	City Events	1	0	0	0
6.01	Arena Fees	1	0	5	1
6.02	Luxury Suite Net Revenue	0	0	6	0
6.04	Allocated Hockey Gross Ticket Revenue	0	0	2	0
7.02	Capital Repairs, Replacements And Improvements	4	8	5	2
8.01	In General (Bank Accounts)	1	0	1	0
8.02	Ticket Account	0	1	0	0
8.03	Bank Account, Records, And Reports	0	0	1	1
9.02	Annual Budgets	0	3	0	1
10.01	Accounting Records And Reports	0	3	4	1
10.02	Annual Financial Statements	0	2	2	1
10.03	Inspection And Audit Rights	0	0	1	1
10.04	Access To Records	0	0	1	2
11.01	General Requirements (With Regards To Insurance)	0	5	0	0
11.02	Property Insurance	5	2	0	3
15.01	On-Site Parking	3	0	0	1
15.02	Off-Site Parking	7	0	0	1
15.04	Responsibilities Of City And Manager	1	0	0	0
18.01	Space For City And Arena Authority Personnel	0	0	0	2
19.01	Luxury Suites	1	0	0	0
19.02	Complimentary Passes And Tickets To City	2	0	0	0
19.03	Parking Passes	1	0	0	0
Attachment #5	Insurance Requirements	23	1	0	0
Attachment #8	Arena Advertising	18	0	0	1
Attachment #11	Advertising Policies	5	0	0	1
Total		90	29	28	22

By performing various additional tasks, the City and the SJAMC can correct current instances of noncompliance with the above terms of the Agreement and help ensure future compliance with those terms.

Section 2.01 - Term

Section 2.01 states, *"Promptly following the Possession Date, the parties shall execute and deliver to each other a memorandum specifying the Possession Date and the end of the Shakedown (45 days after the Possession Date)."* Neither party to the Agreement prepared and delivered a memorandum that stated the possession date or the end of the shakedown period. These dates are important because some of the terms in the Agreement utilize one of those dates, or so many days after one of those dates, as a deadline for a requirement to be met. During the course of our audit, we came across a San Jose Arena Authority (SJAA) memorandum that stated the possession date is August 20, 1993.

We recommend that the City Attorney's Office prepare a memorandum to formally establish August 20, 1993, as the date the SJAMC took possession of the Arena.

Section 3.03 - NBA Or Other Professional Sports Team

In April 1994, the SJAMC announced two new professional sports franchises to the San Jose Arena: the Grizzlies, an indoor soccer team, and the Rhinos, a roller hockey contingent. Section 3.03 of the Agreement states,

Manager shall not enter into an agreement with a . . . professional sports team for use of the Arena as a regular home game facility without City's prior written approval . . .

The SJAMC did not inform the City or request approval for the Grizzlies or the Rhinos as the Agreement requires. In addition, in December 1994, the SJAMC entered into an agreement for the Sabercats, an indoor football team. In this situation, the SJAMC informed the SJAA on December 1, 1994, that the negotiations to have an indoor football team would likely be successful. In its letter the SJAMC requested that the SJAA *"approve SJAMC's request for SJAMC to enter into a Use Agreement . . . for such team to play Arena football . . ."* The SJAMC did not specify in its request the time frame during which an agreement would be entered. On December 5, 1994, the executive director of the SJAA communicated that the SJAA Board of Directors (Board) would hear the item at its regularly scheduled meeting on January 25, 1995. He also stated that since a prompt response was requested he would try to get Board approval via a Unanimous Written Consent. However, the City Attorney's Office stated that due to the limitations of the Brown Act a Unanimous Written Consent was not legal. Therefore, the SJAMC did not receive required City approval for the football team prior to entering into an agreement with the Sabercats.

Furthermore, section 3.03 of the Agreement also states,

. . . City may negotiate with Manager for City to receive additional payments from Manager under this Management Agreement to recover additional costs to City incurred by City in performing its obligations hereunder or resulting directly or indirectly from the use of the Arena by such other professional sports team, . . . and City may withhold or condition its approval of any agreement for use of the Arena by such other professional sports team on additional payments to City for recovery of such additional costs to City to the reasonable satisfaction of City.

In its letter to the City about the potential of an Arena football team, the SJAMC also requested that the SJAA " . . . waive any charges for, or pass through of costs to SJAMC arising from the provision of City off-site traffic control personnel requested or required to staff such Arena Football games at the Arena." According to the executive director of the SJAA, the City and the SJAMC have reached a verbal agreement with regards to who will be responsible for the off-site traffic control costs resulting from any Rhino, Grizzlies, or Sabercat events.

We recommend that the City and the SJAMC formalize any agreement regarding off-site traffic control costs resulting from professional sports events and propose an amendment to section 3.03 of the Agreement to ensure consonance between section 3.03 and any forthcoming written agreement.

Section 4.08 - Maintenance Standard

Section 4.08 describes how the SJAMC should maintain the Arena facilities. This section also requires the SJAMC to prepare and submit to the City, on an annual basis, a detailed programmatic maintenance budget for the Arena facilities including furnishings, fixtures, and equipment. The purpose of the detailed programmatic maintenance budget is to allow for City review to ensure that the SJAMC has complied with the maintenance requirements set forth in this section of the Agreement. In addition, the SJAMC is to submit annually a detailed maintenance performance audit that sets forth the status of maintenance items for the Arena facilities including those furnishings, fixtures, and equipment that were in the budget for the

preceding annual period. The Agreement states that for the first year the maintenance budget was due 90 days after the possession date.

Assuming a possession date of August 20, 1993, the SJAMC should have submitted a maintenance budget to the City on November 18, 1993. For each year thereafter by March 1, the SJAMC should have submitted to the City (1) a detailed programmatic maintenance budget for the following fiscal year and (2) a detailed maintenance performance audit for those items in the previous fiscal years' maintenance budget. The SJAMC has not complied with this requirement for the detailed programmatic maintenance budgets due on March 1, 1994, and March 1, 1995, or the detailed maintenance performance audit which was due on March 1, 1995.

We recommend that the SJAMC immediately prepare a detailed programmatic maintenance budget for 1995-96 and submit it to the City in accordance with the Agreement. Thereafter, the SJAMC should submit to the City a detailed programmatic maintenance budget by March 1 for the following fiscal year and a detailed maintenance performance audit by March 1 for those items in the previous fiscal years' maintenance budget.

Section 4.12 - SJAMC Compliance With Laws, Rules, And Regulations

Section 4.12 of the Agreement states that the SJAMC shall comply with the prevailing wage and hiring requirements set forth in Attachments 9 and 10 of the Agreement. However, a significant portion of the employees working at the Arena work for one of the following four companies with

which the SJAMC has contracted to provide maintenance, concession, security, and cleaning services for the Arena:

- Johnson Controls Worldwide Services, Inc. (maintenance)
- Aramark (concession)
- Staffpro Security, Inc. (security)
- ACME Building Maintenance Co., Inc. (cleaning)

In order to assess compliance with Attachments 9 and 10, we reviewed the SJAMC's personnel manual and the contracts with the above noted entities. Our review revealed noncompliance with some of the terms in Attachments 9 and 10. Appendix C of this report is a summary of the requirements in Attachments 9 and 10 and whether each entity is in compliance with those requirements or not. Based upon our testwork, we noted that the SJAMC personnel manual and the contract with Johnson Controls are not in compliance with the requirements in Attachments 9 and 10. Specifically, neither the SJAMC personnel manual nor the Johnson Controls contract contain any required statements about (1) first source hiring, (2) affirmative action, (3) minority business enterprise/woman business enterprise/disabled business enterprise (MBE/WBE/DBE), (4) prevailing wages, (5) equal employment opportunity (EEO) training, or (6) a policy statement on attempting to expand the pool of qualified female and minority applicants. In addition, the SJAMC personnel manual does not contain any required statements about non-discrimination, outreach programs, or reporting annually to the City Council regarding the gender and ethnic breakdown of the SJAMC's overall workforce. Finally, the Johnson Controls contract does not contain any statements about advertising, all the six requirements listed under affirmative action in Attachment 10, the posting of

notices in conspicuous places regarding discrimination, or the inclusion of a statement regarding EEO in job advertisements.

We recommend that the SJAMC revise, as necessary, its personnel manual and the contract with Johnson Controls to include the Attachments 9 and 10 required statements regarding first source hiring, affirmative action, MBE/WBE/DBE, prevailing wages, outreach programs, EEO training, reporting of gender and ethnic workforce composition, and posting of notices and job advertisements.

Section 7.02 - Capital Repairs, Replacements, And Improvements

Section 7.02 of the Agreement states that

Prior to November 1, of each calendar year, Manager shall prepare and submit to City for its approval a preliminary budget for the following fiscal year which reasonably itemizes and estimates the cost of all Normal Capital Repairs and Replacements and Parking Capital Repairs and Replacements.

The SJAMC has failed to submit a capital budget for 1993-94, 1994-95, and 1995-96. As stated above, a preliminary budget is due on November 1 of each calendar year. The Agreement also states that a final budget is due on March 1 of each year. Without the submittal of a capital budget, the City is unable to review the budget to ensure that it is prepared in accordance with the terms of the Agreement prior to approving the document. In addition, the Agreement states that once the City approves the submitted budget it becomes the official capital budget. Without an official capital budget, the SJAMC cannot make any capital repairs or replacements

other than emergency repairs or replacements, without prior written City approval.

We recommend that the SJAMC immediately prepare and submit for City approval a capital budget for 1995-96 and by November 1, 1995, prepare and submit to the City a preliminary capital budget for 1996-97.

It should be noted that in March 1995 the SJAMC submitted a five-year preliminary capital budget to the City Auditor's office and the SJAA. This five-year preliminary capital budget is from 1994-95 through 1998-99. The SJAMC submitted the five-year preliminary capital budget to solicit any City comments prior to the SJAMC submitting its one-year capital budget to the City for approval as specified in the Agreement.

Based on our review of the preliminary five-year capital budget and the definitions in the Agreement regarding the types of items that should be included in the capital budget, it appears that the SJAMC may have inappropriately included some capital items. Table II is a summary of (1) the total proposed amounts by category the SJAMC included in its five-year preliminary capital budget, (2) the City Auditor's concurrence or nonconcurrence with the preliminary capital budget as submitted, and (3) those items in the preliminary capital budget requiring a City Attorney's Office interpretation.

TABLE II

**SUMMARY OF ANALYSIS CONDUCTED ON REPAIRS
INCLUDED IN PRELIMINARY FIVE-YEAR CAPITAL BUDGET**

Type Of Repair ¹	Total Amount In SJAMC's Preliminary Five-Year Capital Budget ²	City Auditor Concurrence Or Nonconcurrence With The SJAMC's Preliminary Budget		Items In The SJAMC's Preliminary Five-Year Capital Budget That Require Legal Interpretation
		Concurrence	Non-concurrence	
Normal Capital Repairs And Replacement	\$362,500	\$165,000	\$106,500	\$91,000
Parking Capital Repairs And Replacement	28,500	18,500	10,000	
Extraordinary Capital Repairs And Replacement	265,000			265,000
Emergency Capital Repairs And Replacement	70,000	70,000		
Code Changes	126,000	6,000	20,000	100,000
Design And Construction Issues	227,000	77,000	150,000	
Capital Enhancements	191,000	191,000		
Manager's Capital Enhancements	26,000	26,000		
Totals	\$1,296,000	\$553,500	\$286,500	\$456,000

**Nonconcurrence With \$286,500 Of Items
In The SJAMC's Preliminary Five-Year Capital Budget**

As shown in Table II, the City Auditor's Office does not concur with the SJAMC's classification for \$286,500 of the \$1,296,000 in items the

¹ See Appendix E for the detailed breakdown for each of the above-noted repair categories.

² Appendix D of this report shows all the types of repairs, the definitions, and the party responsible for funding the repairs according to the Agreement.

SJAMC included in its preliminary five-year capital budget. The reasons for the City Auditor's nonconcurrence are detailed below.

*Nonconcurrence With \$106,500
Of Normal Capital Repairs And Replacement*

Of the \$106,500 in the Normal Capital Repairs and Replacements category with which we do not concur, \$50,000 appears to be Design And Construction Issues type item, not Normal Capital Repairs and Replacement.

The remaining \$56,500 consists of items that appear to be supplies and equipment as defined in Appendix D. When we raised this issue with SJAMC officials, they responded that the City should continue to be responsible for the type of items for which the Agency paid under the Agreement to Enter. Based on this interpretation, the SJAMC included in its preliminary five-year capital budget items like interior and exterior flags, photocopiers, a facsimile machine, portable radios, and a van. While we understand that the Agency originally purchased these items under the terms of the Agreement to Enter, the City does not appear to be obligated to continually provide funds for these types of items under the terms of the Agreement.

It should be noted that the items discussed above are 1997-98 and 1998-99 capital budget items. Based on the terms of the Agreement, those items that are not part of the current year capital budget are not subject to the City's approval.

We recommend that the City and the SJAMC reach an understanding as to which party will be responsible for the type of equipment items the SJAMC included as 1997-98 and 1998-99 replacement items in its preliminary five-year budget submittal.

*Nonconcurrency With \$10,000
Of Parking Capital Repairs And Replacement*

We also do not concur with the \$10,000 for landscaping that is included in Parking Capital Repairs and Replacements. Specifically, Parking Capital Repairs and Replacements addresses repair and replacement of capital items such as fixtures, machinery, or equipment. In our opinion, landscaping costs do not fit within this definition. Further, Section 4.08 of the Agreement, "Maintenance Standard," states that "*Manager shall maintain the Arena Facilities and landscaping of the Arena Facilities* [Emphasis Added]" Accordingly, we believe landscaping should be part of the general maintenance costs of the Arena and surrounding facilities.

Subsequent to the submittal of its preliminary five-year capital budget, the SJAMC informed the City Auditor's Office that the \$10,000 noted above relates to the replacement of items, such as a tree that had died, within the Arena facilities landscaping.

Nonconcurrency With \$20,000 Of Code Changes

We also do not concur with \$20,000 of items listed in Code Changes. These items are connecting fire phones in the elevators and connecting aisle lights in the lower bowl of the Arena. Based on discussions with the SJAA and the SJAMC, these are items that should have been completed during the construction of the Arena. The codes that require these items were in effect during the design of the Arena. Therefore, these items are Design And Construction Issues type items.

Nonconcurrency With \$150,000

Of Design And Construction Issues

We also do not concur with the \$150,000 for permanent power for the concourse carts that is included in Design and Construction Issues. Under the terms of the Agreement, Design and Construction Issues relate to workmanship deficiencies or premature failures of building components. The issue here is that there are no power outlets on the Arena concourse for concession carts. In our opinion, this item would be more appropriately categorized under Capital Enhancements, which as defined in Appendix D". . . *are made to improve the quality or functioning of the Arena Facilities"*

**\$456,000 Of Items In The SJAMC'S Preliminary
Five-Year Capital Budget Requiring Legal Interpretations**

Also as shown in Table II, the City Auditor's Office has identified \$456,000 of items in the SJAMC's preliminary five-year capital budget that require legal interpretation. The reasons legal interpretations are needed are detailed below.

*\$91,000 Of Normal Capital Repair And
Replacement Items That Require Legal Interpretation*

We question \$91,000 of items that the SJAMC included in its preliminary five-year capital budget for items like Arena floor carpet, cleaning equipment, homosote insulation floor, ice edger, and motorized carts. The SJAMC has stated that the items listed above meet the definition of Normal Capital Repair And Replacement as defined in Appendix D. In our opinion, these terms also appear to fit the definition of supplies and equipment, which states "*All appropriate supplies and equipment for events and for the management and operation of the Arena Facilities shall be*

rented, leased or purchased by Manager at Manager's sole cost and expense."

\$265,000 Of Extraordinary Capital Repairs And Replacement Items That Require Legal Interpretation

We also question \$265,000 of items that the SJAMC included in its preliminary five-year capital budget for hot water heat exchangers and flexible pipe joints. The hot water heat exchangers need to be replaced sooner than their normal life expectancy because of the high mineral content of the water that comes into the Arena. Given this circumstance, a compelling case can be made that the replacement of the heat exchangers could be appropriately categorized either under Normal Capital Repairs and Replacements, Extraordinary Capital Repairs and Replacements, or Design and Construction Issues.

Flexible pipe joints connect pipes, provide sound insulation in piping, and absorb the expansion or contraction of piping. Flexible pipe joints in various areas of the Arena have already failed or have started to leak. Based on what is known about these failures, these repairs could be either an Extraordinary Capital Repair and Replacement, Emergency Capital Repair and Replacement, or a Design and Construction Issue.

\$100,000 Of Code Changes That Require Legal Interpretation

We also question \$100,000 for an item that the SJAMC included in its preliminary five-year capital budget for lower level seating handrails. Based on discussions with the SJAMC, the code that applies to this area is discretionary regarding the installation of handrails. The SJAA and the

SJAMC agree that installing the handrails is appropriate from both a safety and potential liability standpoint. Given this information, this repair could also be classified as a Capital Enhancement.

We recommend that the City, in consultation with the City Attorney's Office, determine the appropriateness of \$456,000 of items that the SJAMC included in its preliminary five-year capital budget.

It should be noted that in Table II, the SJAMC submitted an estimate of \$265,000 for Extraordinary Capital Repairs and Replacements. According to the Agreement, the City is responsible for any costs classified in this category. The City currently is not budgeting for any costs included in this category. The City is budgeting only \$200,000 annually for Normal Capital Repairs and Replacements and Parking Capital Repairs and Replacements. To the extent any of the \$265,000 the SJAMC preliminarily classified as Extraordinary Capital Repairs and Replacements survives the City Attorney's interpretive process, the City will need to budget for these items.

We recommend that the City begin budgeting for the Extraordinary Capital Repairs and Replacements for which it is and will be obligated to pay.

Section 8.02 - Ticket Account

Section 8.02 of the Agreement states,

On or before the Possession Date, Manager shall establish one trust or escrow account with the ticket agency or agencies that will sell tickets to Arena events to the public (the "Ticket Account"). Using receipts

from the sale of the first tickets sold for events at the Arena (other than Hockey) Manager shall deposit and maintain in the Ticket Account an amount equal to the gross receipts that would be received from the sale of all tickets to one Arena event, such as a rock concert or family show, assuming the tickets are priced in accordance with the industry standard for such events and the event is sold out, but excluding any tickets attributable to seats in Executive Suites.

To date, the SJAMC has not established a ticket account. According to the SJAMC, this provision was added to the contract to ensure that if a promoter or program backs out of its commitment to perform, there would be a pool of money from which refunds could be made to ticket holders. The SJAMC feels that this account is unnecessary for two reasons. The first reason is that for every program held at the Arena, the SJAMC prepares an Arena Use Agreement. In this Use Agreement, section 9, entitled "Ticket Sales," states the following: *"All ticket revenues shall be the sole property of SJAMC until box office settlement in accordance with Section 11 below."* Section 11, entitled "Box Office Settlement," states that

Within twenty-four (24) hours after the conclusion of the Program, SJAMC shall furnish the Licensee with a box office statement and, at the Licensee's request, make a provisional settlement with the Licensee, with SJAMC withholding such sums from such provisional settlement as it deems, in its sole discretion, required to assure proper final settlement.

Based on this information, the SJAMC has possession of all ticket revenue until the program has taken place.

The second reason the SJAMC feels that the ticket account is unnecessary is because of an operating account reserve. Specifically, the SJAMC represented to the City Auditor's Office that its operating account always has enough money to more than cover any needed refunds.

The preceding two justifications notwithstanding, the SJAMC has not opened the required ticket account and is therefore out of compliance with section 8.02 of the Agreement.

We recommend that the SJAMC either open the ticket account to be in compliance with section 8.02 of the Agreement or propose an amendment to the Agreement to remove this requirement.

Section 9.02 - Annual Budgets

Section 9.02 of the Agreement states that the SJAMC will provide for each fiscal year of the Agreement (1) a program operating budget; (2) a maintenance budget described in section 4.08 (see page 15); and (3) a detailed line-item facility improvements budget for capital enhancements.

Based on our review of the Agreement, we were unable to find a definition for the program operating budget.

We recommend that the City and the SJAMC agree on a definition of what the program operating budget in section 9.02 of the Agreement should include in order to facilitate the SJAMC preparing the budget and submitting it to the City for review and approval in accordance with the terms of the Agreement.

Capital enhancements are expenditures that are made to improve the quality or functioning of the Arena facilities. The SJAMC did include a list of capital enhancements as part of the preliminary five-year capital budget it

submitted in March 1995 (see page 20). However, to date, the SJAMC has not provided any budgets to the City for review and approval.

We recommend that the SJAMC submit to the City for review and approval a capital enhancement budget in accordance with section 9.02 of the Agreement.

Section 10.01 - Accounting Records And Reports

Section 10.01 of the Agreement states that the systems and procedures the SJAMC uses to maintain its accounting records shall include a system of internal controls that shall be divided between the activities and operations in which the City has a direct financial interest versus those areas in which the City has no direct financial interest. Any area where the City has a financial interest is called a "City-Related Account." The City-related accounts are the reserve fund, the ticket account, the expenditures described in the budgets discussed in sections 7.02 and 9.02 of the Agreement, and all the items of income and expenditures that are used to calculate luxury suite net revenue and hockey ticket revenue.

Currently, the only City-related accounts where this requirement would apply are the ticket account and the budgets discussed in sections 7.02 and 9.02 of the Agreement. As we have noted on pages 18, 25, and 27 of this report, the SJAMC has not complied with the requirements of these two areas. Therefore, the City has not had the system of internal controls described to it or received or reviewed any detailed records and reports related to these accounts. As a result, the City has not been able to verify

that an adequate audit trail exists for all the income and expenses affecting the City-related accounts.

In addition, in our opinion, based on our review and discussions with the vice president and chief financial officer (CFO) of the SJAMC, the documentation of the SJAMC's system of internal controls and procedures is deficient. The CFO stated that he plans on performing a complete review of all the accounting cycles (revenue, expenses, and payroll) in conjunction with the next financial statement audit which will occur in September 1995. According to the CFO, his review will facilitate the SJAMC documenting its system of internal controls and procedures and help resolve the noncompliance issue noted above. It should be noted that the CFO did provide us with the SJAMC's outside auditors' most recent internal control review which addressed the following areas:

- Merchandising/Retail Operations/Concession Sales
- Ticket Sales
- Parking Revenues
- Suite Revenue
- Advertising/Broadcasting Revenue
- Purchasing/Accounts Payable/Cash Disbursements
- Payroll

The SJAMC's outside auditors noted for all the areas listed above that, in general, controls appeared adequate. While they did note some areas where improvements could be made, they did not find any material weaknesses in the SJAMC's internal control structure.

We recommend that the SJAMC adequately document its system of internal controls and procedures that impact the City-

related accounts in order to facilitate the City's right to have access to, review, and verify the financial information that supports the City-related accounts.

Section 10.02 - Annual Financial Statements

Section 10.02 of the Agreement states that the SJAMC shall provide, at its expense, statements of income and expense for the City-related accounts every fiscal year, accompanied by an unqualified opinion from an outside auditor (Auditor). The Auditor's opinion must contain a statement with respect to the calculation of the City-related accounts for the fiscal year subject to audit. The Auditor must be a certified public accountant that is licensed to practice in the state of California. The SJAMC has the right to select the Auditor; however, the City must approve of the selection. In addition to the documents noted above, the Auditor must provide a certificate stating that the calculation of the City-related accounts is *"fairly presented in accordance with the terms and provisions of this Management Agreement."* This document is called the "City Income Report" in the Agreement. The Agreement also states that the SJAMC shall deliver the audit report and City income report to the City within 90 days of the close of the fiscal year. The close of the fiscal year is July 31; therefore, the reports noted must be delivered by October 29 annually.

As we stated earlier in this report, the only City-related accounts where section 10.02 would apply are the ticket account (section 8.02.) and the budgets (sections 7.02 and 9.02). As we previously noted, the SJAMC has not complied with the requirements of sections 7.02, 8.02, and 9.02.

Consequently, the City has (1) yet to receive an audit report or City income report and (2) been precluded from exercising its right to inspect or audit the financial records pertaining to the City-related accounts.

We recommend that once the SJAMC is in compliance with sections 7.02, 8.02, and 9.02, it provide the City with an audit report and City income report in accordance with section 10.02 of the Agreement.

Section 11.01 - General Requirements Regarding Insurance

Section 11.01 of the Agreement states that the SJAMC shall purchase and maintain in full force and effect during the term of the Agreement insurance policies in accordance with Attachment 5 of the Agreement. Based on our review of the SJAMC's insurance coverage, we noted that some verbage from the endorsement requirements is not included in its coverage. Specifically, the SJAMC's policy does not include either the SJAA as an insured or the required statement "*. . . its employees, officers, agents and contractors are hereby added as insureds as respects the use, operation and maintenance of the facilities.*"

In addition, section 11.01 also states that the SJAMC

. . . shall cause its tenants, concessionaires, service contractors and others using or performing work or services in or about the Arena Facilities to procure and maintain policies of insurance with the same coverages (but not necessarily the same amounts, in Manager's reasonable judgment) as set forth in Attachment No. 5.

Based upon our review of the insurance requirements listed in each subcontractor agreement, we noted that Aramark, who provides concession

services, is not in compliance with the insurance requirements set forth in Attachment 5 of the Agreement. Specifically, the Aramark contract does not include:

- \$5,000/\$25,000 limits for medical coverage;
- Neither the Agency nor the SJAA are listed as insureds; and
- Items #2, #3, and #4 listed under "Endorsements" are not included.

We recommend that the SJAMC amend its insurance policy to include the appropriate language for insureds and its contract with Aramark to incorporate the insurance requirements that are not included in the current contract.

Section 11.02 - Property Insurance

Section 11.02 of the Agreement addresses the level of property insurance both the City and the SJAMC must carry, along with various other requirements. Based upon our review of both the City's and the SJAMC's policies, we noted two areas of noncompliance.

The first area of noncompliance is the requirement that the City provide the SJAMC with copies of the insurance policies applicable to this section in a form reasonably satisfactory to the SJAMC. As of September 1, 1995, the City has not provided the SJAMC with copies of the required insurance policies.

The second area of noncompliance is the requirement that the City carry business income insurance, at the SJAMC's expense, to insure the business losses of the SJAMC in the event of damage to the Arena facilities. The Agreement also states that the City will bill the SJAMC for the increase in the premium attributable to the business income insurance coverage. To date, the City has paid \$15,584 in premiums for business income insurance.

The Agreement also states that the City shall bill and the SJAMC shall pay within 30 days of receipt, but no more than 10 days prior to the date the premium is due, the amount the City incurs as a result of carrying the business income insurance.

We recommend that the City provide the SJAMC with copies of the required insurance policies and bill the SJAMC for \$15,584 in premiums incurred on behalf of the SJAMC.

Environmental Compliance And Remediation

During the course of our audit, the SJAMC expressed concern over the issue of environmental compliance and remediation of hazardous substances present at the Arena facilities. Based on our review of the Agreement, there is no mention of which party is responsible for the remediation or monitoring of hazardous substances on site. However, the Agreement to Enter (construction agreement) states the following as it relates to hazardous substances on-site:

. . . SJ³ shall be responsible for Investigation and Remediation of any Hazardous Substances now present in, on or under or Released onto, in, under, over, from or about the Arena Site . . . including those Hazardous Substances known by SJ to presently exist on the Arena Site as of the date of this Agreement to Enter, and including all costs associated with all Investigation and Remediation performed or required hereunder to be performed by SJ. SJ shall implement and complete the current and, using reasonable good faith efforts, any future Investigation and Remediation for which SJ is responsible hereunder, . . .

³ SJ is defined as " . . . collectively, the City and Agency, or either of them as the case may be."

In addition, the Cooperation Agreement entered into by the Agency and the City on March 20, 1995, states

Agency shall pay any and all costs in connection, or associated with . . . (ii) any and all expenses of remediation due to ground water or soil contamination and remediation, except as may be directly caused by the negligence of Manager or City.

Finally, the Agreement to Enter also states that the SJAMC is responsible for the investigation and remediation of any hazardous substances on the Arena site that arise from the actions of the SJAMC or others acting under the SJAMC's control, supervision, authority or permission.

We recommend that the City and the San Jose Arena Management Corporation amend the Management Agreement to include a section that identifies which party is responsible for environmental compliance and remediation of hazardous substances located on the Arena site.

CONCLUSION

Based upon our audit of the compliance requirements contained in the San Jose Arena Management Agreement, we noted 90 instances of compliance, 29 instances of noncompliance, and 28 terms for which compliance needs to occur at a future date. By implementing the recommendations in this report, both the City and the San Jose Arena Management Corporation can ensure compliance with the terms set forth in the Management Agreement.

RECOMMENDATIONS

We recommend that the City Attorney's Office:

Recommendation #1:

Prepare a memorandum to formally establish August 20, 1993, as the date the San Jose Arena Management Corporation took possession of the Arena. (Priority 3)

In addition, we recommend that the City and the San Jose Arena Management Corporation:

Recommendation #2:

Formalize any agreement regarding off-site traffic control costs resulting from professional sports events and propose an amendment to section 3.03 of the Management Agreement to ensure consonance between section 3.03 and any forthcoming written agreement. (Priority 2)

Recommendation #3:

Reach an understanding as to which party will be responsible for the type of equipment items the San Jose Arena Management Corporation included as 1997-98 and 1998-99 replacement items in its preliminary five-year budget submittal. (Priority 2)

Recommendation #4:

Agree on a definition of what the program operating budget in section 9.02 of the Management Agreement should include in order to facilitate the San Jose Arena Management Corporation preparing the budget and

submitting it to the City for review and approval in accordance with the terms of the Management Agreement. (Priority 2)

Recommendation #5:

Amend the Management Agreement to include a section that identifies which party is responsible for environmental compliance and remediation of hazardous substances located on the Arena site. (Priority 2)

Furthermore, we recommend that the San Jose Arena Management Corporation:

Recommendation #6:

Immediately prepare a detailed programmatic maintenance budget for 1995-96 and submit it to the City in accordance with the Management Agreement. Thereafter, the San Jose Arena Management Corporation should submit to the City a detailed programmatic maintenance budget by March 1 for the following fiscal year and a detailed maintenance performance audit by March 1 for those items in the previous fiscal years' maintenance budget. (Priority 2)

Recommendation #7:

Revise, as necessary, its personnel manual and the contract with Johnson Controls to include the Attachments 9 and 10 required statements regarding first source hiring, affirmative action, minority business enterprise/ woman business enterprise/disabled business enterprise (MBE/WBE/DBE), prevailing wages, outreach programs, equal employment opportunity (EEO) training,

reporting of gender and ethnic workforce composition, and posting of notices and job advertisements. (Priority 2)

Recommendation #8:

Immediately prepare and submit for City approval a capital budget for 1995-96 and by November 1, 1995, prepare and submit to the City a preliminary capital budget for 1996-97. (Priority 2)

Recommendation #9:

Either open the ticket account to be in compliance with section 8.02 of the Management Agreement or propose an amendment to the Management Agreement to remove this requirement. (Priority 2)

Recommendation #10:

Submit to the City for review and approval a capital enhancement budget in accordance with section 9.02 of the Management Agreement. (Priority 2)

Recommendation #11:

Adequately document its system of internal controls and procedures that impact the City-related accounts in order to facilitate the City's right to have access to, review, and verify the financial information that supports the City-related accounts. (Priority 2)

Recommendation #12:

Once it is in compliance with sections 7.02, 8.02, and 9.02, provide the City with an audit report and City income report in accordance with section 10.02 of the Management Agreement. (Priority 2)

Recommendation #13:

Amend its insurance policy to include the appropriate language for insureds and its contract with Aramark to incorporate the insurance requirements that are not included in the current contract. (Priority 2)

Finally, we recommend that the City:

Recommendation #14:

In consultation with the City Attorney's Office, determine the appropriateness of \$456,000 of items that the San Jose Arena Management Corporation included in its preliminary five-year capital budget. (Priority 2)

Recommendation #15:

Begin budgeting for the extraordinary capital repairs and replacements for which it is and will be obligated to pay. (Priority 2)

Recommendation #16:

Provide the San Jose Arena Management Corporation with copies of the required insurance policies and bill the San Jose Arena Management Corporation for \$15,584 in premiums incurred on behalf of the San Jose Arena Management Corporation. (Priority 2)

OTHER PERTINENT INFORMATION

Luxury Suite Net Revenue Sharing

Commencing with the beginning of the fourth hockey season (1996-97), the city of San Jose (City) will receive 20 percent of Luxury Suite Net Revenue from the San Jose Arena Management Corporation (SJAMC). The SJAMC is required to pay and remit to the City an estimated amount beginning August 1, 1996.

The following table shows the description of the calculation to determine Luxury Suite Net Revenue from the San Jose Arena Management Agreement (Agreement) and the City Auditor's Office comments to clarify the various steps of the calculation:

TABLE III

DISCUSSION AND COMMENTS REGARDING LUXURY SUITE NET REVENUE CALCULATION

Luxury Suite Net Revenue Calculation Description From The Agreement

. . . Luxury Suite Net Revenue . . . shall mean proceeds from sales or rentals of Luxury Suites (prorated annually, in an equal amount attributable to each year of such sale or rental, in the case of proceeds received for more than one year) less:

(a) amounts included in such proceeds representing the price of hockey tickets included as part of the sale or rental package (provided that for purposes of this deduction, the price for such hockey tickets shall not exceed the highest price charged for the sale of such tickets other than as part of a luxury suite or club seat package), and

City Auditor's Office Comments

The Arena has 64 luxury boxes. The SJAMC enters into leases with suite holders for various time frames. If a lease is entered into for three years and the total amount of the lease is received in year one, the amount received will be prorated over the lease term for purposes of the revenue sharing calculation.

According to this section, the value of the hockey tickets has to be deducted from the amount paid for the luxury suites. The amount of the hockey tickets will be included in the allocated hockey gross ticket revenue calculation in the eleventh hockey season.

Luxury Suite Net Revenue Calculation
Description From The Agreement

City Auditor's Office Comments

(b) Luxury Suite Costs.

Luxury Suite Costs shall, as applicable, for all Luxury Suites, including the following:

- (a) all of Manager's and Shark's "Hard Costs" and "Soft Costs" (as defined in Attachment No. 6 of the Agreement to Enter), attributable to the build out of the Sky Boxes or upgrade of finishes in the Concourse Boxes, as determined, amortized over twelve (12) years on a level payment basis at the greater of 10.25% per annum, simple interest, or the rate per annum, plus interest, actually charged by a lender advancing funds for purposes of such build-out, such amortization to be determined as if it commenced on the first day of August of the fourth Hockey Season, regardless of when the costs were actually incurred or the actual period during which such costs are amortized . . .*

- (b) Hard and Soft Costs to Manager or Sharks of major repairs, replacements, and refurbishments amortized based in accordance with generally accepted accounting principles; and*

- (c) reasonable commissions not exceeding amounts actually paid to salespersons; provided such commissions do not exceed those customarily paid by arenas meeting the Applicable Standard.*

Hard and soft costs are defined in the Agreement to Enter as follows:

Hard Costs: All sums paid or payable to contractors or suppliers for construction or purchase and installation of items of the Arena Facilities, including costs of so-called "turnkey" contracts, purchases of good and services, purchases of labor and materials, fees (including inspection, testing and plan check, and permit fees), taxes, bonds and insurance included in prices charged by such contractors and suppliers.

Soft Costs: All sums paid or payable to third-party professionals (design, architectural, engineering) for design or descriptive work for the Arena facilities, preparation of plans and bid specifications, change orders, and construction-related supervision and inspection and testing. Excluded are costs of attorneys, managers, employees, consultants and agents, and administrative and overhead costs of San Jose and Manager.

The applicable standard is defined in the Agreement as ". . . a standard of performance, operation (including bookings), maintenance equal to or exceeding those generally applicable to contemporary comparable major arenas in the United States at which NBA and/or NHL games are played (such as Target Center, Palace at Auburn Hills, Phoenix Suns Arena and Bradley Center)."

During the course of our audit, we requested, and the SJAMC did not provide, (1) gross Luxury Suite Net Revenues and (2) hard and soft costs as defined in the Agreement to Enter as shown in Table III.

Therefore, we were unable to determine whether the SJAMC will be able to comply with the Agreement provisions regarding Luxury Suite Net Revenue which go into effect on August 1, 1996.

Preventative Maintenance

Article 4 of the Agreement discusses the general duties of the SJAMC. Section 4.01 states that the SJAMC shall undertake and perform certain services and responsibilities to the extent they are necessary and appropriate and consistent with the terms and purposes of the Agreement and City policies and guidelines. Of those responsibilities, two are (1) the development of a preventative and major maintenance plan and (2) the preparation of maintenance reporting systems.

Preventative maintenance is generally defined as "*. . . a program in which wear, tear, and change are anticipated and continuous corrective actions are taken to ensure peak efficiency and minimize deterioration. It involves a planned and controlled program of systematic inspection, adjustment, lubrication, replacement of components, as well as performance testing and analysis.*" The primary objective of a preventative maintenance program is the reduction in downtime of vital systems and equipment. In addition, a successful preventative maintenance program has many benefits, almost all of which have some type of cost savings. Finally, a preventative maintenance program extends the life of the facilities and equipment, improves equipment reliability, will ensure that the equipment is operating properly, and will improve safety by identifying and quickly correcting unsafe conditions.

Based on our review of the Agreement, there are no specific requirements or guidelines as to the format, content, or a date of completion for the documents and systems noted. As of September 1, 1995, the SJAMC had not prepared a preventative and major maintenance plan. However, the contractor responsible for the maintenance function in the Arena implemented a maintenance reporting system on January 1, 1995.

On June 27, 1995, the City entered into a contract with Aztec Consultants/MCE Corporation (Consultants) to provide assistance in the oversight of the maintenance program at the Arena. The scope of services is broken into three phases:

- Phase I -** Design and development of a Facilities Maintenance Oversight System for the Arena as a pilot project for the City under the direction of the San Jose Arena Authority (SJAA).
- Phase II -** Implementation and operation of the Facilities Maintenance Oversight System for the Arena.
- Phase III -** Continuing services and expansion of the Facilities Maintenance Oversight System in other City-maintained facilities.

Phases I and II will focus on the Arena.

Phase I

Phase I includes the following steps:

- Project orientation
- Document existing practices
- Work activity analysis

- Inventory and condition assessment
- Levels of service objectives
- Work activity guides
- Preventative maintenance task lists
- Annual work program and budget
- Work distribution
- Capital improvements recommendations (optional)

Phase II

Phase II includes the following steps:

- Scheduling and reporting procedures
- Data processing support
- Quarterly facility inspections
- Systems evaluation and improvement (optional)

Based upon the scope of services with the Consultants, the City will be better able to ensure that the SJAMC is maintaining the Arena properly and in accordance with the terms of the Agreement.

It should be noted that the SJAA has requested the Consultants' assistance with a number of repair issues that are not within the scope of services discussed above. Specifically, the Consultants have assisted the SJAA with the following issues: (1) chiller failure, (2) flexible connectors, (3) various water leaks, particularly the roof and atrium area, and (4) basketball and multi-purpose room buildout. In addition, a letter dated September 6, 1995, from Johnson Controls to the SJAA stated the following:

... be advised there are several issues that should be addressed before the start of hockey season to avoid the possibility of business interruption or potential liability.

- 1. Connect Fire phones in elevators.**
- 2. Connect aisle lights. (lower bowl seating)**
- 3. Replace domestic hot water heat exchangers.**
- 4. Replacement of Mason flexible pipe joints.**
- 5. Water supply isolation/bypass valve.**
- 6. Cooling tower isolation valve.**
- 7. Repair Santa Clara street sanitary sewer main.*
- 8. Repair concrete settlement North entrance steps.*
- 9. Roof, glass and other various water leaks.*

The SJAMC has expressed a desire to meet with the SJAA and the Consultants to discuss an action plan to resolve the above-noted issues.

[Click On The Appropriate Box To View Item](#)

Administrator's Response

Appendix A

Appendix B

Appendix C

Appendix D

Appendix E

Appendix F

* These items are included in the preliminary five-year capital budget that the SJAMC submitted in March 1995 and are discussed on pages 22, 24, and E-2 of this report.